

Office of the State Auditor

Division of State Audit

Insurance Department Bismarck, North Dakota

Audit Report for the
Biennium Ended June 30, 2007
Client Code 401

Robert R. Peterson
State Auditor



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Transmittal Letter

March 17, 2007

The Honorable John Hoeven, Governor

Members of the North Dakota Legislative Assembly

The Honorable Adam Hamm, Commissioner, Insurance Department

We are pleased to submit this audit of the Insurance Department for the biennium ended June 30, 2007. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Allison Bader. Andrea Wike and Kristi Morlock were the staff auditors. Fred Ehrhardt, CPA, was the audit supervisor and Paul Welk, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 328-2320. We wish to express our appreciation to Commissioner Hamm and his staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

Robert R. Peterson
State Auditor

Executive Summary

INTRODUCTION

The North Dakota Insurance Department is a state regulatory agency headed by the Insurance Commissioner. The Insurance Commissioner provides a variety of services including agent licensing and investigation, consumer protection, financial examinations, and company licensing services. The Insurance Commissioner administers various special funds and programs including the State Fire and Tornado Fund, State Bonding Fund, Petroleum Tank Release Compensation Fund, Boiler and Anhydrous Ammonia Facility Inspection Program, State Health Insurance Counseling Program, and Prescription Connection for ND Program.

RESPONSES TO LAFRC AUDIT QUESTIONS

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

1. What type of opinion was issued on the financial statements?

Financial statements were not prepared by the Insurance Department in accordance with generally accepted accounting standards so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Other than our finding addressing "Noncompliance with Procurement Policies" (see page 18), the Insurance Department was in compliance with significant statutes, laws, rules, and regulations under which it was created and is functioning.

3. Was internal control adequate and functioning effectively?

Other than our findings addressing the "Inadequate Controls Surrounding Investments" (see page 11), "Segregation of Duties Surrounding Accounts Receivable" (see page 12), "Inadequate Controls Surrounding Payroll" (see page 13), and "Lack of General Ledger Transaction Approval Procedures" (see page 14), we determined internal control was adequate.

4. *Were there any indications of lack of efficiency in financial operations and management of the agency?*

Other than our work addressing "Investment Procedure Improvements" (see page 19) and "Information Systems Managing Accounts Receivable" (see page 20), there were no indications of lack of efficiency in financial operations and management of the Insurance Department.

5. *Has action been taken on findings and recommendations included in prior audit reports?*

The Insurance Department has implemented all recommendations included in the prior audit report.

6. *Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.*

Yes, a management letter was issued and is included on page 21 of this report, along with management's response.

LAFRC AUDIT COMMUNICATIONS

1. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified or significant unusual transactions.

2. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The Insurance Department's financial statements do not include any significant accounting estimates.

3. *Identify any significant audit adjustments.*

Significant audit adjustments were not necessary.

4. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

5. *Identify any serious difficulties encountered in performing the audit.*

None.

6. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

7. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

8. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance, Human Resource Management System (HRMS), Deposit System, Fire and Tornado, Fire District, and Boiler and Anhydrous Ammonia Inspection Program are high-risk information technology systems critical to the Insurance Department.

Background Information

The Insurance Department is a state regulatory agency headed by the Insurance Commissioner. The Insurance Department is responsible for the regulation of insurance companies and agents doing business in the state of North Dakota. The Commissioner licenses both resident and non-resident agents and has the responsibility of approving instructional courses for credit and monitoring agents' compliance with the continuing education requirements. The Commissioner manages the ND State Fire and Tornado Fund, the State Bonding Fund, the Unsatisfied Judgment Fund, the Insurance Regulatory Trust Fund, and the Petroleum Tank Release Compensation Fund.

The Insurance Department has six main divisions:

Insurance Department includes the following divisions:

- Legal & Enforcement
 - Consumer Protection
 - Examinations and Company Licensing
 - Agent Licensing and Investigation
 - Administration
 - Special Funds
-

The Legal and Enforcement Division works with the investigators of the Insurance Department to enforce the laws applicable to insurance agents and insurance companies doing business in the state. The Division also advises Department staff about laws, administrative rules, and the implementation of agency policy.

The Consumer Protection Division includes the Life and Health, and Property and Casualty Consumer Protection Divisions. These Divisions review policy forms to ensure policy language complies with all the laws of the state, properly reflects the benefits provided by the policy, and is not deceptive or misleading. Within the Consumer Protection - Life and Health Division is the State Health Insurance Counseling (SHIC) Program, which works with trained volunteers throughout the state to help senior citizens with questions about Medicare and related health insurance policies. Also within the Consumer Protection – Life and Health Division is the Fraud Investigation Unit available for the public to report fraudulent insurance acts and the Prescription Connection for ND that connects qualified people with discount drugs direct from the manufacturer.

The Examinations and Company Licensing Division licenses insurers to sell insurance in North Dakota. The Division conducts regular financial examinations and analysis of insurance companies to ensure solvency.

The Agent Licensing and Investigation Division licenses agents doing business in the state. This Division is assigned all duties necessary to carry out the issuing, renewal, and ongoing processing of agent licensing, including license applications, renewals, agent appointments, continuing-education filing reports, and course approval for continuing education courses. The

investigations area of the Division is responsible for conducting agent and company investigations on behalf of the public. This includes handling all consumer complaints regarding agents, and life-and-health complaints against insurance companies to ensure the fair treatment of policyholders.

The Administration Division is responsible for oversight of the accounting budget, information-technology needs, and general office support for the Department.

The Special Funds Division is comprised of the various special funds and programs under the authority of the Insurance Commissioner. These funds include:

The State Fire and Tornado Fund which insures buildings and contents belonging to state agencies and political subdivisions.

The State Bonding Fund provides a blanket fidelity bond for state agencies and political subdivisions providing coverage in the event of employee theft of property or money.

The Petroleum Tank Release Compensation Fund which accounts for clean-up costs associated with underground petroleum tank spills.

The Boiler and Anhydrous Ammonia Facility Inspection Program included in the Fire and Tornado Fund provides mechanical inspection of boilers and pressure vessels and their components.

The Insurance Department's budget for the 2005-2007 biennium totals \$13.7 million. This represents less than a 1.5% increase over the 2003-2005 budget. Special and federal fund sources comprise the 2005-2007 biennium budget for the Insurance Department.

More information about the agency can be obtained from the Insurance Department's home page at:

<http://www.state.nd.us/ndins/>.

Audit Objectives, Scope, And Methodology

Audit Objectives

The objectives of this audit of the Insurance Department for the biennium ended June 30, 2007 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the most important areas of the Insurance Department's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the Insurance Department and are they in compliance with these laws?
3. Are there areas of the Insurance Department's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of the Insurance Department for the biennium ended June 30, 2007 was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. To meet the objectives outlined above, we:

Audit Methodology

- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and developed a discussion and analysis of the financial statements.
- Performed detailed analytical procedures for expenditures and receipts.
- Tested samples of receipts, expenditures, journal vouchers, and correcting entries.
- Reviewed prior year audit workpapers.
- Interviewed appropriate agency personnel.
- Reviewed Insurance Department written plans and applicable manuals.
- Reviewed Insurance Department's biennial report.
- Observed Insurance Department's processes and procedures.
- Reviewed North Dakota Century Code title 26.1, chapter 23-37, and 2005 Session Laws.
- Conducted review of processes for receipting revenue to manage accounts receivable within information systems.
- Reviewed processes and procedures for investing special funds with the State Investment Board.
- Conducted review of processes and procedures for providing bonding coverage to state entities and political subdivisions.

Discussion And Analysis

The accompanying financial statements have been prepared to present the Insurance Department's revenues and expenditures on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the biennium ended June 30, 2007, operations of the Insurance Department were primarily supported by fees and fines credited to the Insurance Regulatory Trust fund. This is supplemented by appropriations from the Insurance Tax Distribution Fund, federal funding, and other income credited to the agency's Petroleum Tank Release Compensation, Bonding, and Fire and Tornado Funds.

FINANCIAL SUMMARY

Revenues consisted primarily of collections of insurance and fire and tornado premium taxes. Other revenues during the audited period included various fees and fines collected from examinations, licensing agents and insurance companies, and Petroleum Tank Fund registrations. Revenues remained fairly constant during the audit period. Total revenues were \$43,845,976 for the year ended June 30, 2007 as compared to \$41,364,361 for the year ended June 30, 2006.

Total expenditures for the Insurance Department were \$13,588,196 for the year ended June 30, 2007 as compared to \$13,211,688 for the prior year. Grants, benefits, and claims related to distributions to fire districts and loss claims, as well as legislative transfers to the general fund account for approximately 64% of total expenditures.

The Insurance Department has agency fund deposits of securities held in custody for domestic life insurance companies in accordance with NDCC 26.1-05-23. Amounts held in custody totaled \$2,261,894 at June 30, 2007 and 2006, respectively. These funds are not reported on the financial statements as the securities are held in a trust capacity for the insurance companies.

Financial Statements

STATEMENT OF REVENUES AND EXPENDITURES

	<u>June 30, 2007</u>	<u>June 30, 2006</u>
<u>Revenues and Other Sources:</u>		
Insurance Premium Tax	\$30,168,197	\$29,124,817
Fire and Tornado Collections	4,846,628	4,997,408
Insurance Agent Fees	3,083,662	3,066,665
Insurance Company Fees	1,995,653	1,232,092
Federal Revenue	170,350	222,200
Other Fees	857,638	808,422
Other Revenue	98,559	46,855
Transfers In	2,625,288	1,865,901
Total Revenues and Other Sources	<u>\$43,845,976</u>	<u>\$41,364,361</u>
<u>Expenditures and Other Uses:</u>		
Salaries and Benefits	\$2,273,664	\$2,171,211
Major Operating Expenses:		
Grants, Benefits, and Claims	6,509,688	6,466,050
Insurance	1,434,993	1,330,076
Travel	146,246	139,257
Professional Services	122,980	356,030
IT Data Processing	121,220	155,219
Rent/Lease-Building/Equipment	99,484	127,449
Postage	50,166	51,023
IT Communications	35,105	34,023
Printing	33,014	37,073
Professional Development	28,471	37,443
Equipment under \$5,000	32,165	16,006
Supplies	39,847	38,759
Other Expenses	25,410	144,884
Transfers Out	2,635,743	2,107,185
Total Expenditures and Other Uses	<u>\$13,588,196</u>	<u>\$13,211,688</u>

STATEMENT OF APPROPRIATIONS

For The Biennium Ended June 30, 2007

Expenditures by Line Item:	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Benefits	\$ 5,096,278		\$ 5,096,278	\$ 4,429,452	\$ 666,826
Operating Expenses	2,163,377	\$ 15,000	2,178,377	1,454,401	723,976
Grants	6,420,000		6,420,000	6,420,000	
Totals	<u>\$ 13,679,655</u>	<u>\$ 15,000</u>	<u>\$ 13,694,655</u>	<u>\$ 12,303,852</u>	<u>\$ 1,390,803</u>
Expenditures by Source:					
Other Funds	\$ 13,679,655	\$ 15,000	\$ 13,694,655	\$ 12,303,852	\$ 1,390,803
Totals	<u>\$ 13,679,655</u>	<u>\$ 15,000</u>	<u>\$ 13,694,655</u>	<u>\$ 12,303,852</u>	<u>\$ 1,390,803</u>

Appropriation Adjustments:

The increase in the Operating Expenses line (\$15,000) increased spending authority to accept funds from the Insurance Regulatory Trust fund to reimburse outstanding claims for locking devices related to the Critical Methamphetamine-Use Zone identified by House Bill 1010 Section 10 of the 2005 Legislative Assembly.

Expenditures Without Appropriations Of Specific Amounts:

Unsatisfied Judgment Fund – Court approved judgments have a continuing appropriation as authorized by NDCC section 26.1-23-01. (\$40,000)

Bonding Fund – Claims-related expenditures have a continuing appropriation in accordance with NDCC section 26.1-21-02. (\$373,317)

Fire and Tornado Fund – Claims-related expenditures have a continuing appropriation in accordance with NDCC section 26.1-22-13. (\$8,277,181)

Petroleum Tank Release Compensation Fund – Claims paid out have a continuing appropriation as authorized by NDCC section 23-37-29. (\$1,428,716)

Insurance Regulatory Trust Fund – Legislative non-appropriated transfers to the general fund authorized by NDCC section 26.1-01-07.1. (\$4,376,818)

Internal Control

In our audit for the biennium ended June 30, 2007, we identified the following areas of the Insurance Department's internal control as being the most important:

Internal Controls Subjected To Testing

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the computer-based Boiler and Anhydrous Ammonia Inspection, Petroleum Tank, Deposit, Fire and Tornado, and Fire District programs.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered significant. We concluded that internal control was not adequate noting certain matters involving internal control and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect Insurance Department's operations or ability to record, process, summarize, and report financial data consistent with the assertions of management in financial statements. Reportable conditions are described below. We also noted other matters involving internal control that we have reported to management of the Insurance Department in a management letter dated March 17, 2007.

Finding 07-1

INADEQUATE CONTROLS SURROUNDING INVESTMENTS

During our review of investment procedures, we noted controls surrounding the movement of investment funds are not adequate.

The Insurance Department maintains four money market demand accounts (MMDA) for the bonding, fire and tornado, petroleum tank, and insurance regulatory trust funds. The Insurance Department uses these accounts as clearing accounts for transferring investment funds between the State Treasurer and the State Investment Board (SIB). Checks are processed from the State Treasurer and the MMDAs several times a month. The Insurance Department has granted the authority to initiate movement of funds between the State Treasurer and the MMDAs maintained at the BND to an individual who also has access to cash and reconciles investment accounts.

According to the Committee of Sponsoring Organizations (COSO) *Internal Control – Integrated Framework Executive Summary*, segregation of duties is a control activity used to ensure necessary actions are taken to address an entity's operating risks. Properly designed segregation of duties requires segregation between individuals that initiate transactions, have access to cash, and perform reconciliation procedures.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Insurance Department properly segregate duties surrounding investments related to initiating movements of funds, having access to cash and reconciling accounts.

Insurance Department Response:

The Insurance Department concurs with the recommendation. The four money market demand accounts (MMDA) have been eliminated. Funds are now being transferred between the State Investment Board (SIB) and the State Treasurer electronically eliminating access to these funds by Insurance Department staff. Job duties of Department staff have been reassigned to ensure proper segregation of duties.

Finding 07-2

SEGREGATION OF DUTIES SURROUNDING ACCOUNTS RECEIVABLE

During our review of accounts receivable at the Insurance Department, we noted control procedures are not adequate.

The individual assigned to post debits and credits to accounts and prepare billings for the Petroleum Tank and Bonding funds collections also opens the mail, endorses checks, prepares the remittance listing, and performs data entry of revenue into the Insurance Department's deposit information system and Connect ND Financials.

According to the Committee of Sponsoring Organizations (COSO) *Internal Control – Integrated Framework Executive Summary*, segregation of duties is a control activity used to ensure necessary actions are taken to address an entity's operating risks. Properly designed segregation of duties requires an individual independent of billing and maintaining accounts receivable records receive or handle revenue collections.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Insurance Department properly segregate duties surrounding accounts receivable by ensuring an individual independent of access to cash maintain accounts receivable and prepare billings.

Insurance Department Response:

The Insurance Department concurs with the recommendation. Job duties of Department staff have been reassigned to ensure proper segregation of duties.

Finding 07-3

INADEQUATE CONTROLS SURROUNDING PAYROLL

During our review of payroll processes and procedures, we identified the following weaknesses surrounding control activities and monitoring of payroll:

- the individual assigned responsibility to approve the monthly payroll register also has access to payroll records on ConnectND Human Resource Management System (HRMS);
- the personnel action forms (PAF) are not reconciled to the initiating form; and
- the ConnectND one-time payment query, which summarizes all one-time payments processed through ConnectND HRMS, is not reviewed by the Insurance Department.

According to the Committee of Sponsoring Organizations (COSO) *Internal Control – Integrated Framework Executive Summary*, segregation of duties, reconciliations, and approvals are control activities used to ensure necessary actions are taken to address an entity's operating risks. Properly designed control activities surrounding payroll require:

- an individual independent of access to update payroll records, approve the payroll register;
- an individual independent of data entry for personnel action form (PAF) information reconcile the updated PAF to the initiating form; and
- the ConnectND HRMS one-time payment query be reviewed for unusual transactions and approved by an appropriate level of management on a regular basis.

Audit Recommendation
and Agency Response

Recommendation:

We recommend the Insurance Department strengthen controls surrounding payroll by:

- a. Ensuring an individual independent of access to update payroll records on ConnectND HRMS approves the payroll register.

- b. Assigning responsibility to reconcile the personnel action forms (PAF) to the initiating form to an individual independent of payroll data entry.
- c. Implementing procedures to ensure the ConnectND one-time payment query is reviewed and approved by an appropriate level of management on a regular basis.

Insurance Department Response:

- a. The Insurance Department concurs with the recommendation. Job duties of Department staff have been reassigned to ensure an individual independent of access to update payroll records on ConnectND HRMS approves the payroll register.
- b. The Insurance Department concurs with the recommendation. Job duties of Department staff have been reassigned to ensure an individual independent of payroll data entry reconciles the personnel action forms (PAF) to the initiating form.
- c. The Insurance Department concurs with the recommendation. Procedures have been implemented to ensure that the ConnectND one-time payment query is reviewed and approved on a regular basis.

Finding 07-4

LACK OF GENERAL LEDGER TRANSACTION APPROVAL PROCEDURES

The ConnectND general ledger did not have online approval capabilities for journal entries during our audit period, and the Insurance Department did not have documented approval of transactions processed through the general ledger.

According to the Committee of Sponsoring Organizations (COSO) Internal Control – Integrated Framework Executive Summary, verifications and approvals are control activities used to ensure necessary actions are taken to address an entity's operating risks. Properly designed internal controls require the review and approval of all accounting transactions. Journal entries that are not reviewed and approved have a greater risk of errors or irregularities.

Audit Recommendation and
Agency Response

Recommendation:

We recommend the Insurance Department establish procedures to confirm approval of ConnectND General Ledger transactions.

Insurance Department Response:

The Insurance Department concurs with the recommendation. Procedures have been implemented to ensure that general ledger transactions are approved by an appropriate level of management.

Compliance With Legislative Intent

In our audit for the biennium ended June 30, 2007, we identified and tested Insurance Department's compliance with legislative intent for the following areas that we determined to be significant and of higher risk of noncompliance:

Legislative Intent Subjected To Testing

- Deposit and allocation of Petroleum Release Compensation fund registration fees (NDCC 23-37-15, 23-37-29, 23-37-17).
- Collection and allocation of fees (NDCC 26.1-01-07, 26.1-01-07.1).
- Investment activity (NDCC 26.1-07-07.2).
- Proper deposit of map fees (NDCC 26.1-01-07.5).
- Collection and allocation of premium tax (NDCC 26.1-03-17).
- Deposit and allocation of examination fees (NDCC 26.1-03-19.6).
- Collection of premiums – State Bonding Fund (NDCC 26.1-21-09).
- Allocation of Fire and Tornado Fund (NDCC 26.1-22-02, 26.1-22.1-13).
- Collection and allocation of Fire and Tornado Fund reserve (NDCC 26.1-22-14, 26.1-22-15).
- Collection and allocation of boiler inspection fees (NDCC 26.1-22.1-09, 26.1-22.1-10).
- Allocation of Unsatisfied Judgment Fund (NDCC 26.1-23-01).
- Collection of accreditation of continuing or prelicensure education fee (NDCC 26.1-26-31.3).
- Appraisal of state-owned property insured by the Fire and Tornado Fund (NDCC 26.1-22-06.1).
- Procurement of excess loss reinsurance (NDCC 26.1-22-21).
- Collection of viatical settlement provider and broker license application fee (NDCC 26.1-33.2-02).
- Collection of nonresident insurance producer continuation fee (NDCC 26.1-26.20).
- Appropriations and related transfers (2005 North Dakota Session Laws Chapter 10).

- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with OMB's Purchasing Procedures Manual.
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper use of outside bank accounts and proper authority for investments outside the Bank of North Dakota.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with fixed asset requirements including record keeping, surplus property, lease and financing arrangements in budget requests, and lease analysis requirements.
- Compliance with payroll related laws including certification of payroll.

The results of our tests disclosed one instance of noncompliance that is required to be reported under *Government Auditing Standards*. This finding is described below. Other than this finding, we concluded there was compliance with the legislative intent identified above. We also noted certain immaterial instances of noncompliance that we have reported to management of the Insurance Department in a management letter dated March 17, 2007.

NONCOMPLIANCE WITH PROCUREMENT POLICIES

Finding 07-5

The Insurance Department does not have control procedures in place to properly monitor compliance with State Procurement Office procurement policies, and as a result, improper procurement procedures were used to purchase services and items greater than \$2,500.

- State Procurement Office (SPO) Procurement Manual Section 6.1 states that for purchases between \$2,500 and \$25,000, solicitation of no fewer than three vendors shall be made, insofar as practical, to submit oral or written informal bids or proposals. If the three bids or proposals are not received, written justification is required. Four instances were noted where the Insurance Department did not document the proper number of informal bids.
- SPO Procurement Manual Section 3.2 states that emergency purchases must be made with the level of competition practicable under the circumstances. A written determination of the basis for the emergency and selection of the particular contractor must be included in the contract file. An Emergency Purchase Determination form must be completed and promptly forwarded to the OMB State Procurement Office after the purchase has been made. Three instances were noted where the Insurance Department did not properly document the basis for emergency purchases and contractor selection and notify OMB of the purchases.
- Per SPO Procurement Manual Section 2.2, officers of procurement shall maintain courteous, professional relationships with all vendors, and avoid any activities, relationships, and communications that in any way diminish, or appear to diminish, fair and impartial treatment of vendors. One instance was noted where the Insurance Department did not provide comparative information to all vendors.

Audit Recommendation and Agency Response

Recommendation:

We recommend the Insurance Department implement an adequate review process by an individual knowledgeable of the procurement policies to establish proper procurement procedures and documentation in compliance with State Procurement Office Guidelines.

Insurance Department Response:

The Insurance Department concurs with the recommendation. Procedures have been put in place to ensure compliance with State Procurement Office Guidelines. Included in those

procedures is additional training for Department staff and the appointment of procurement officers to oversee the Departments procurement activities.

Operations

Our audit of the Insurance Department identified the following areas of potential improvements to operations:

Operational
Improvement 07-1

INVESTMENT PROCEDURE IMPROVEMENTS

Background:

The Insurance Department is responsible for investing monies with the State Investment Board (SIB). The Insurance Department's process passes investment monies from the State Treasurer through four money market demand clearing accounts (MMDA): Bonding, Fire and Tornado, Petroleum Tank, and Insurance Regulatory Trust to the SIB. Investment funds are electronically transferred between the MMDAs and the SIB; however, the Insurance Department processes and hand delivers numerous checks several times a month when transferring monies between the State Treasurer and the MMDAs. In addition, the Insurance Department maintains a separate investment transaction register for reconciling purposes. Request and approval procedures are performed for all movements of investment funds.

Operational Improvements:

According to the Committee of Sponsoring Organizations (COSO) Internal Control – Integrated Framework Executive Summary, the assurance of objectives achieved through properly designed internal control include efficiency of operations. Consultation with the Office of Management and Budget and the Office of the State Treasurer verified that maintaining MMDAs as clearing accounts for investing funds with the SIB is not required and creates inefficiency. Funds can be transferred directly from the Office of State Treasurer to the SIB. By discontinuing maintenance of the MMDAs, processing checks, maintaining the manual investment transaction register and performing additional approval procedures related to the MMDAs would be eliminated within the investment process.

Recommendation:

We recommend the Insurance Department perform investment transactions through electronic transfer between the State Treasurer and the State Investment Board.

Insurance Department Response:

The Insurance Department concurs with the recommendation. The four money market demand accounts (MMDA) have been eliminated. Funds are now being transferred between the State Investment Board (SIB) and the State Treasurer electronically.

***INFORMATION SYSTEMS MANAGING ACCOUNTS
RECEIVABLE***

Background:

The Insurance Department maintains an Oracle database deposit system and information subsystems to manage receivables related to fire and tornado, company licensing, petroleum tank, and boiler inspection accounts. Collections are manually entered into the deposit system daily and then subsequently manually entered into each applicable subsystem to update the accounts receivables. The Insurance Department also utilizes Excel to manage additional account information for company licensing. Reconciliations are required between the deposit system and the subsystems as well as ConnectND Financials and the fire and tornado subsystem to ensure proper entry of transactions applied to accounts.

Operational Improvement:

According to the Committee of Sponsoring Organizations (COSO) Internal Control – Integrated Framework Executive Summary, the assurance of objectives achieved through properly designed internal control include efficiency of operations. Implementing a synchronized process to record collections entered in the deposit system to electronically update the accounts receivable managed in the subsystems would eliminate the inefficient need to re-enter collections. Developing the company licensing information subsystem to manage all account information would eliminate maintenance of a separate Excel spreadsheet.

Recommendation:

We recommend the Insurance Department explore the possibility of interfacing the deposit system with information subsystems utilized to manage accounts receivable.

We also recommend the Insurance Department identify the necessary company licensing information managed in Excel and implement changes to utilize the Company Licensing subsystem to manage companies.

Insurance Department Response:

The Insurance Department concurs with the recommendation. The Department is currently evaluating alternative databases that incorporate a deposit system for agent licensing, company licensing, form/rate filing and premium tax collection. The systems being considered are web based and offered by the National Association of Insurance Commissioners. They would offer integration at an affordable price. At this time the new system being considered will not meet the needs of the Special Fund Division. The Department will continue to look for ways to improve or replace the subsystems being used by the Special Funds Division. The modification of those systems to meet this recommendation is cost prohibitive and would require additional appropriation from the legislature.

Management Letter (Informal Recommendations)

March 17, 2007

Honorable Adam Hamm, Commissioner
Insurance Department
State Capitol
600 E. Boulevard Avenue
Bismarck, ND 58505

Dear Commissioner Hamm:

We have performed an audit of the Insurance Department for the biennium ended June 30, 2007, and have issued a report thereon. As part of our audit, we gained an understanding of the Insurance Department's internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status as non-reportable conditions.

The following present our informal recommendations.

INVESTMENTS

Informal Recommendation 07-1: We recommend the Insurance Department establish proper review procedures to ensure investment transactions are properly coded on ConnectND to the investment asset accounts.

ACCOUNTS PAYABLE/EXPENDITURES

Informal Recommendation 07-2: We recommend the Insurance Department implement proper approval procedures of transactions processed through the ConnectND Financial Accounts Payable module for proper identification of the approver within ConnectND.

REVENUE

Informal Recommendation 07-3: We recommend the Insurance Department assign an individual independent of Deposit System data entry and revenue deposit preparation to reconcile the deposit on the Deposit System to ConnectND Financials revenue on a regular basis. We also recommend the ConnectND Financials deposit journal entry reconciliation include review and approval of coding as to fund, account and class.

Informal Recommendation 07-4: We recommend the Insurance Department develop a documented policy for credit card procedures including an approval process and review of refunds and credit card activity for reasonableness and any unusual patterns.

LEGISLATIVE INTENT

Informal Recommendation 07-5: We recommend the Insurance Department establish proper procedures to notify the Office of Management and Budget of the fiscal year-end mandatory transfer authorized by NDCC 26.1-01-07.1 section 3 for proper CAFR presentation in accordance with generally accepted accounting principles.

Informal Recommendation 07-6: We recommend the Insurance Department comply with OMB Policy and OMB Purchase Card Manual requirements when making purchases using the state procurement card.

INFORMATION SYSTEMS

Informal Recommendation 07-7: We recommend the Insurance Department:

- a. Restrict access privileges for the ConnectND GL data entry and FOCUS Boiler Inspection system to individuals necessary to perform assigned responsibilities.
- b. Assign responsibility for reviewing security privileges on a regular basis for all information systems utilized by the Department.

OPERATIONAL

Informal Recommendation 07-8: We recommend the Insurance Department include the website address for the Department in the review process for the development of brochures to provide valuable program information to the public.

Informal Recommendation 07-9: We recommend the Insurance Department ensure all bonding policies remain in force until cancelled or changed by the bond holder. We also recommend the Insurance Department update bonding application guidelines to include limits to the amount of coverage available by the bonding fund.

Management of Insurance Department agreed with these recommendations.

I encourage you to call myself or an audit manager at 328-2241 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

Allison Bader
Auditor in-charge